

SPENCER MUNICIPAL UTILITIES
INDEPENDENT AUDITORS' REPORTS
FINANCIAL STATEMENTS
AND SUPPLEMENTAL INFORMATION
DECEMBER 31, 2007 AND 2006

TABLE OF CONTENTS

	<u>Page</u>
Officials	1
 Municipal Electric Utility:	
Independent Auditors' Report	2
Management's Discussion and Analysis	3 - 5
 Financial Statements:	
Balance Sheets	6 - 7
Statements of Revenues, Expenses and Changes in Fund Net Assets	8
Statements of Cash Flows	9 - 10
Notes to Financial Statements	11 - 21
 Supplemental Information:	
Budgetary Reporting	22 - 24
 Independent Auditors' Report on Compliance and Internal Control Over Financial Reporting	
	25 - 26
Schedule of Findings	27 - 28
 Municipal Water Utility:	
Independent Auditors' Report	29
Management's Discussion and Analysis	30 - 32
 Financial Statements:	
Balance Sheets	33 - 34
Statements of Revenues, Expenses and Changes in Fund Net Assets	35
Statements of Cash Flows	36 - 37
Notes to Financial Statements	38 - 46
 Supplemental Information:	
Budgetary Reporting	47 - 49
 Independent Auditors' Report on Compliance and Internal Control Over Financial Reporting	
	50 - 51
Schedule of Findings	52 - 53

TABLE OF CONTENTS - Continued

	<u>Page</u>
Municipal Communications Utility:	
Independent Auditors' Report	54
Management's Discussion and Analysis	55 - 57
Financial Statements:	
Balance Sheets	58
Statements of Revenues, Expenses and Changes in Fund Net Assets	59
Statements of Cash Flows	60 - 61
Notes to Financial Statements	62 - 68
Supplemental Information:	
Budgetary Reporting	69 - 71
Independent Auditors' Report on Compliance and Internal Control Over Financial Reporting	72 - 73
Schedule of Findings	74 - 75

SPENCER MUNICIPAL UTILITIES

OFFICIALS

DECEMBER 31, 2007

<u>Board of Trustees</u>		<u>Term Expires</u>
Tom Howe	Trustee	6-30-2008
Bruce Tamisiea	Chairman	6-30-2010
Dave Hultgren	Vice-Chairman	6-30-2011
Gary Tolzmann	Secretary	6-30-2012
Murray Hart	Treasurer	6-30-2013
<u>Management</u>		
Leon Rodas	General Manager	
Steven Pick	Business Manager	

THIS PAGE INTENTIONALLY LEFT BLANK

SPENCER MUNICIPAL UTILITIES

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA**

THIS PAGE INTENTIONALLY LEFT BLANK

INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Electric Utility
Spencer, IA 51301

We have audited the accompanying balance sheets of the Municipal Electric Utility of the City of Spencer, Iowa (the Utility) as of December 31, 2007 and 2006, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Utility's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Utility as of December 31, 2007 and 2006, and the respective changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 10, 2008 on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis and budgetary comparison information on pages 3 through 6 and 23 through 25 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurements and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 10, 2008

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of management's discussion and analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Electric Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the year ended December 31, 2007.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2007 Financial Highlights

The Utility delivered approximately 162,700,000 kilowatt hours (kWh) of electricity to its retail customers in 2007 compared to approximately 159,121,000 kWh in 2006.

The Utility's net assets increased \$1,504,514 to \$48,059,392 as a result of operations for the year ended December 31, 2007.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Balance Sheet

	<u>2007</u>	<u>2006</u>
Current assets	\$7,926,371	\$2,327,888
Capital assets, net of depr.	39,536,253	37,110,284
Noncurrent assets	14,038,952	21,384,467
Deferred costs	<u>139,910</u>	<u>154,234</u>
Total assets	<u>61,641,486</u>	<u>60,976,873</u>
Current liabilities	2,267,094	2,081,995
Long-term debt	<u>11,315,000</u>	<u>12,340,000</u>
Total liabilities	<u>13,582,094</u>	<u>14,421,995</u>
Investments in capital assets, net of related debt	27,336,163	23,939,518
Restricted	2,466,710	2,467,845
Unrestricted	<u>18,256,519</u>	<u>20,147,515</u>
Total net assets	<u>48,059,392</u>	<u>46,554,878</u>
Total liabilities and net assets	<u>\$61,641,486</u>	<u>\$60,976,873</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Sales of electricity	\$10,162,968	\$10,174,902
Other	<u>600,084</u>	<u>163,665</u>
Total operating revenue	<u>10,763,052</u>	<u>10,338,567</u>
Power supply costs	6,431,178	6,114,337
Distribution system maintenance	1,308,819	1,229,262
Depreciation & amortization	2,140,122	1,796,460
Customer service & administration	<u>844,773</u>	<u>725,187</u>
Total operating expenses	<u>10,724,892</u>	<u>9,865,246</u>
Operating income (loss)	38,160	473,321
Interest income	1,020,997	1,157,578
Interest expense	(449,602)	(332,973)
Other income	<u>894,959</u>	<u>675,978</u>
Total non-operating revenues	<u>1,466,354</u>	<u>1,500,583</u>
Change in net assets	1,504,514	1,973,904
Net assets, beginning of year	<u>46,554,878</u>	<u>44,580,974</u>
Net assets, end of year	<u>\$48,059,392</u>	<u>\$46,554,878</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Financial Analysis

The Utility's total assets increased by approximately \$664,000.

The Utility's gross revenues increased by approximately \$424,000 or 4.11%.

Power supply costs have increased by approximately \$317,000. The remaining operating expenses increased by approximately \$542,000 due to increased expenses related to distribution maintenance, customer accounting and collections expenses, and administrative expenses. Depreciation and amortization also increased by approximately \$343,000.

Total operating income generated in 2007 was \$38,160 compared to \$473,321 in 2006.

Utility non-operating income (expense) resulted in an additional \$1,466,354 of income due to additional leases of utility facilities.

Total net income (loss) decreased from \$1,973,904 in 2006 to \$1,504,514 in 2007

Capital Assets and Debt Administration

Net capital assets increased by approximately \$2,426,000 due to the completion of construction of the Walter Scott, Jr Energy Center #4 (formerly the Council Bluffs Energy Center Unit), distribution construction, and equipment purchases.

During December of 2007, the Board of Trustees entered a joint ownership agreement for the construction of the Sutherland Generating Station Unit 4. The Utility will become an approximately 1.0% owner which is 8 megawatts. The Utility's total ownership interest is estimated at \$19,480,000.

Economic Factors

The Utility continues to experience stability in retail sales. In order to cover more of its baseload capacity, the Board of Trustees has entered into a joint ownership agreement for the construction of the Sutherland Generating Station Unit 4.

The utility adopted an Energy Cost Adjustment (ECA) for all consumption beginning September 7, 2005. The ECA is calculated monthly and is designed to recoup the additional costs of power supply from the consumer.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Business Manager, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

THIS PAGE INTENTIONALLY LEFT BLANK

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BALANCE SHEETS
DECEMBER 31, 2007 AND 2006**

	2007	2006
ASSETS		
Capital Assets:		
Plant in Service	\$ 68,425,666	\$ 53,249,118
Accumulated Depreciation	(29,005,756)	(26,995,655)
Net Plant in Service	39,419,910	26,253,463
Land	86,092	86,092
Construction in Progress	30,251	10,770,729
Total Capital Assets	39,536,253	37,110,284
Noncurrent Assets		
Restricted Cash and Cash Equivalents		
Restricted	131,125	130,865
Consumer Deposits	22,626	20,931
Noncurrent Investments:		
Unrestricted	(2,167,129)	2,967,095
Board Designated	10,381,000	10,381,000
Restricted	2,335,585	2,336,980
Notes Receivable - Employees	328	1,596
Notes Receivable - City of Spencer	335,417	-
Notes Receivable -Municipal Communications Utility	3,000,000	5,546,000
Total Noncurrent Assets	14,038,952	21,384,467
Current Assets:		
Cash and Cash Equivalents		
Unrestricted	4,106,536	(1,391,933)
Board Designated	1,275,971	1,255,630
Accounts Receivable (Net of Allowance for Doubtful		
Accounts of \$75,000 and \$30,000)	904,549	960,394
Unbilled Usage	459,152	464,538
Materials And Supplies Inventory	573,450	609,399
Fuel Inventory	310,755	182,623
Notes Receivable - City of Spencer	25,000	26,625
Notes Receivable - Employees	3,880	4,378
Prepayments and Other	267,078	216,234
Total Current Assets	7,926,371	2,327,888
Deferred Costs:		
Unamortized Bond Issue Costs	139,910	154,234
Total Assets	\$ 61,641,486	\$ 60,976,873

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BALANCE SHEETS
DECEMBER 31, 2007 AND 2006**

	2007	2006
LIABILITIES AND NET ASSETS		
Bonds Payable:		
Bonds Payable	\$ 12,340,000	\$ 13,325,000
Less - Current Maturities	(1,025,000)	(985,000)
Total Bonds Payable	<u>11,315,000</u>	<u>12,340,000</u>
Current Liabilities:		
Accounts Payable	907,439	796,665
Payroll and Sales Tax Payable	47,972	42,421
Accrued Payroll and Compensated Absences	214,020	188,206
Accrued Interest Payable	50,037	48,772
Consumer Deposits	22,626	20,931
Current Maturities of Long-Term Debt	1,025,000	985,000
Total Current Liabilities	<u>2,267,094</u>	<u>2,081,995</u>
Total Liabilities	<u>13,582,094</u>	<u>14,421,995</u>
Net Assets		
Invested in Capital Assets, Net of Related Debt	27,336,163	23,939,518
Restricted	2,466,710	2,467,845
Unrestricted	18,256,519	20,147,515
Total Net Assets	<u>48,059,392</u>	<u>46,554,878</u>
Total Liabilities and Net Assets	<u><u>\$ 61,641,486</u></u>	<u><u>\$ 60,976,873</u></u>

THIS PAGE INTENTIONALLY LEFT BLANK

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	2007	2006
Operating Revenues:		
Residential	\$ 3,466,208	\$ 3,413,558
Commercial	4,869,916	4,694,434
Public Authorities	564,656	649,182
Sales for Resale	565,148	123,038
Energy Cost Adjustment Revenue	1,262,188	1,417,728
Penalties	20,316	17,189
Miscellaneous	14,620	23,438
Total Operating Revenues	10,763,052	10,338,567
Operating Expenses:		
Generation and Transmission		
Neal #4 Fuel and Generation	928,639	784,865
Walter Scott #4 Fuel and Generation	555,811	-
Purchased Power	4,879,598	5,211,987
Other	67,130	117,485
Distribution	1,308,819	1,229,262
Depreciation and Amortization	2,140,122	1,796,460
Customer Operations	282,749	258,304
General and Administrative	562,024	466,883
Total Operating Expenses	10,724,892	9,865,246
Operating Income	38,160	473,321
Non-Operating Income (Expense):		
Interest Income on Investments	1,020,997	1,157,578
Economic Development Payment	(35,005)	(44,036)
Leased Facilities	1,539,754	1,156,112
Interest Expense	(449,602)	(332,973)
Loss on Plant Retirements	(72,622)	(14,478)
Payment in Lieu of Property Taxes	(537,168)	(421,620)
Total Non-Operating Income (Expense)	1,466,354	1,500,583
Change in Net Assets	1,504,514	1,973,904
Net Assets at Beginning of Year	46,554,878	44,580,974
Net Assets at End of Year	\$ 48,059,392	\$ 46,554,878

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	<u>2007</u>	<u>2006</u>
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 10,825,979	\$ 10,240,449
Cash Payments to Suppliers for Goods and Services	(8,058,504)	(8,101,516)
Cash Payments to Employees for Services	(536,210)	(514,461)
Payments Received From Leasing of Facilities	1,539,754	1,156,112
Net Cash Provided By Operating Activities	<u>3,771,019</u>	<u>2,780,584</u>
Cash Flows From Noncapital Financing Activities:		
Contributions Paid for Economic Development	(35,005)	(44,036)
Payment in Lieu of Property Taxes	(537,168)	(421,620)
Net Cash (Used) By Noncapital Financing Activities	<u>(572,173)</u>	<u>(465,656)</u>
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(4,630,248)	(7,404,549)
Revenue Bond Principal Repayment	(985,000)	(955,000)
Interest Paid	(448,337)	(335,827)
Net Cash (Used) By Capital and Related Financing Activities	<u>(6,063,585)</u>	<u>(8,695,376)</u>
Cash Flows From Investing Activities:		
Payments Received on Note Receivable -City of Spencer	41,208	26,625
Loan Advances for Note Receivable -City of Spencer	(375,000)	-
Payments Received on Note Receivable Employee	5,376	10,661
Loan Advances for Note Receivable Employee	(3,610)	(11,755)
Payments Received on Note Receivables - Communications	2,546,000	1,000,000
Proceeds From Redemption of Investments	14,850,901	8,738,543
Purchase of Investments	(9,715,282)	(16,162,720)
Proceeds from Sale of Capital Assets	14,914	-
Interest Received From Investments	1,020,997	1,157,578
Net Cash Provided (Used) By Investing Activities	<u>8,385,504</u>	<u>(5,241,068)</u>
Net Increase (Decrease) in Cash	5,520,765	(11,621,516)
Cash at Beginning of Year	<u>15,493</u>	<u>11,637,009</u>
Cash at End of Year	<u>\$ 5,536,258</u>	<u>\$ 15,493</u>
Reconciliation:		
Cash and Cash Equivalents		
Unrestricted	\$ 4,106,536	\$ (1,391,933)
Board Designated	1,275,971	1,255,630
Restricted	131,125	130,865
Consumer Deposits	22,626	20,931
	<u>\$ 5,536,258</u>	<u>\$ 15,493</u>

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	2007	2006
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating Income	\$ 38,160	\$ 473,321
Adjustments to Reconcile Operating Income to Net Cash Provided By Operating Activities		
Depreciation and Amortization	2,140,122	1,796,460
Leased Facilities Income	1,539,754	1,156,112
(Increase) Decrease in Operating Assets:		
Accounts Receivable	55,844	(80,266)
Unbilled Usage	5,386	(19,273)
Materials and Supplies Inventory	35,949	(34,262)
Fuel Inventory	(128,132)	(48,353)
Prepayments	(50,844)	(147,193)
Increase (Decrease) in Operating Liabilities:		
Accounts Payable	101,720	(267,596)
Accrued Payroll and Compensated Absences	25,814	(47,578)
Consumer Deposits	1,695	1,421
Accrued Expenses	5,551	(2,209)
Total Adjustments	<u>3,732,859</u>	<u>2,307,263</u>
Net Cash Provided By Operating Activities	<u>\$ 3,771,019</u>	<u>\$ 2,780,584</u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Electric Utility of the City of Spencer, Iowa (Electric Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Water Utility and the Municipal Communication Utility of the City of Spencer, Iowa, by a five member Board of Trustees.

The Utility follows the accounting practices prescribed through the Federal Energy Regulatory Commission for regulated utilities and proprietary fund accounting for governmental entities under accounting principles generally accepted in the United States of America.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Boards has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes. An audit of the City of Spencer for the year ended June 30, 2007 has been completed and is filed under separate cover.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Boards Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new electric facilities. In addition, net interest costs on construction debt are capitalized. During 2007, the Utility capitalized interest expense of \$137,981.

Under a joint ownership agreement with other utilities, the Electric Utility has a 1.215% undivided interest in a 644 MW electric generation station known as George Neal Generating Station Unit No. 4. The Electric Utility's 1.215% ownership interest in this plant represents a total investment of \$4,844,778 included in utility plant in service with \$3,688,837 included in accumulated depreciation. Operating costs associated with this plant and depreciation are reflected in the statement of income.

Under a joint ownership agreement with other utilities, the Electric Utility has a 1.07% undivided interest in a 790 MW electric generation station known as Walter Scott, Jr. Energy Center Unit 4, which was placed in service in 2007. The Electric Utility's 1.07% ownership interest in this plant represents a total investment of \$14,221,849 included in utility plant in service with \$210,336 included in accumulated depreciation. Operating costs associated with this plant and depreciation are reflected in the statement of income.

Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred.

Depreciation is provided on a straight-line basis. Current depreciation expense is approximately 3.36% of the original cost of depreciable electric plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	20-33 years
Building and improvements	20 years
Equipment	5 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to valuation allowance based on its assessment the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Bond Issue Costs

Unamortized debt issue costs are amortized over the life of the debt on a straight-line basis which approximates the effective interest method.

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent proceeds. Net assets are reported as restricted when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

G. Income Taxes

The Electric Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of electricity. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2007, totaled \$459,152.

I. Estimates

The preparation of the financial statements in conformity in U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS

The Utility's deposits in Banks at December 31, 2007 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies, and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

The Utility had investments in Iowa Public Agency Investment Trust which are valued at an amortized cost of \$2,497,966 in pursuant to Rule 2a-7 under the Investment Company Act of 1940.

Interest Rate Risk – The Utility's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

Credit Risk – The Utility's investment in the Iowa Public Agency Investment Trust is unrated.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

Investments are recorded at cost which approximates market. Adjustments are made to cost for any premium or discount, which is amortized over the maturity of the investment. Adjustments are also made to account for the change in accrued interest on respective investments.

Reconciliation of the Utility's cash and cash equivalents and noncurrent investments is as follows:

	2007	2006
Cash and cash equivalents:		
Board designated	\$ 1,275,971	\$ 1,275,630
Consumer Deposits	22,626	20,931
Restricted	131,125	130,865
Unrestricted	4,106,536	(1,391,933)
Total cash and cash equivalents	5,536,258	15,493
Noncurrent investments:		
Unrestricted	(2,167,128)	2,967,095
Board designated	10,381,000	10,381,000
Restricted	2,335,585	2,336,980
Total noncurrent investments	10,549,457	15,685,075
Total cash and cash equivalents and noncurrent investments	\$ 16,085,715	\$ 15,700,569

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 3 - BOARD DESIGNATED FUNDS

The Board of Trustees of the Utility has designated certain funds to be placed in a contingency reserve account. These funds, which are from unrestricted net assets, are being designated for contingencies such as a natural disaster, and cannot be expended without Board approval.

The Board of Trustees of the Utility has designated certain funds to be placed in a replacement and construction reserve account. These funds, which are from unrestricted net assets, are being designated for replacement of property, plant and equipment and for new construction. These funds cannot be expended without Board approval.

Assets of the funds as of December 31, 2007 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Cash and cash equivalents	\$ 1,275,971	\$ -	\$ 1,275,971
Noncurrent investments	-	10,381,000	10,381,000
Total	\$ 1,275,971	\$ 10,381,000	\$ 11,656,971

Note 4 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2007 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 86,092	\$ -	\$ -	\$ 86,092
Construction in progress	10,770,729	3,481,371	(14,221,849)	30,251
Total capital assets not being depreciated	10,856,821	3,481,371	(14,221,849)	116,343
Capital assets being depreciated:				
Infrastructure	46,884,808	15,226,524	(66,774)	62,044,557
Buildings and improvements	765,876	-	(89,634)	676,242
Equipment	5,598,434	152,326	(45,893)	5,704,867
Total capital assets being depreciated	53,249,117	15,378,850	(202,301)	68,425,666
Less accumulated depreciation	26,995,655	2,125,798	(115,697)	29,005,756
Total capital assets being depreciated - net	26,253,463	13,253,052	(86,604)	39,419,910
Capital assets - net	\$37,110,284	\$16,734,423	\$ (14,308,453)	\$39,536,253

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 5 - NOTES RECEIVABLE – EMPLOYEES

The Board of trustees has authorized the Electric Utility to purchase personal computers for interested employees. The employees repay the Utility through payroll withholding over a maximum of 24 months. No interest is charged on the unpaid balance.

Note 6 - TRANSFERS IN LIEU OF PROPERTY TAXES/NOTE RECEIVABLE

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Currently, transfers approximate 5% of gross sales (excluding the energy cost adjustment), less actual property taxes paid (on the George Neal Generating Station Unit No. 4) and returned to the City of Spencer, Iowa. Additionally, funds declared to be surplus can be, and have been, transferred to the City.

During 1996, the Utility advanced the City \$355,000, of which \$266,250 was a loan, to perform public improvements in the area of West 11th Street in Spencer. The City reimburses the Utility in equal payments of \$26,625 without interest, payable annually on July 1. The last payment was made during the year.

During 2007, the Utility loaned the City \$375,000 to fund the economic development loan to Shine Bros. Corp. The City reimburses the Utility in equal payments of \$2,083 without interest, payable monthly. The balance of this note at December 31, 2007 was \$360,417.

Note 7 - NOTE RECEIVABLE – MUNICIPAL COMMUNICATIONS UTILITY

The Board of Trustees has approved an \$8,000,000 line of credit for the Municipal Communications Utility for use in start-up and construction costs related to bringing the Communications Utility into operation. The balance of the line of credit at December 31, 2007 was \$3,000,000. Outstanding balances bear interest at a rate of 4 5% per annum.

Note 8 – BONDS PAYABLE

Bonds payable activity for the year ended December 31, 2007 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Series 2000 revenue bonds	\$5,545,000	\$ -	\$ 490,000	\$5,055,000	\$ 515,000
Series 2004 revenue bonds	7,780,000	-	495,000	7,285,000	510,000
Total revenue bonds	<u>\$13,325,000</u>	<u>\$ -</u>	<u>\$ 985,000</u>	<u>\$12,340,000</u>	<u>\$1,025,000</u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 8 – BONDS PAYABLE (Continued)

The Series 2000 and 2004 revenue bonds require annual principal payments, due December 1, and semiannual interest payments, due June 1 and December 1. Interest rates throughout the term of the bonds range between 1.4% and 5.75 %. The bonds are secured by the future net revenues of the Utility. Long-term debt matures and bears interest as follows:

	Series 2000		Series 2004	
	Principal	Interest	Principal	Interest
2008	\$ 515,000	\$ 282,343	\$ 510,000	\$ 265,567
2009	545,000	254,018	520,000	253,583
2010	575,000	224,042	535,000	239,802
2011	610,000	192,418	550,000	224,288
2012	645,000	158,868	565,000	206,687
2013-2017	2,165,000	251,403	3,155,000	708,460
2018-2019	-	-	1,450,000	95,650
Total	\$ 5,055,000	\$ 1,363,090	\$ 7,285,000	\$ 1,994,037

The bond resolutions provide certain covenants relating to the collection, segregation, and distribution of revenues from customers; places certain restrictions on future borrowing and leasing or disposition of assets; and requires that minimum insurance coverage be maintained.

Restricted Funds

Outstanding Electric Revenue Bonds are collateralized by the revenue of the Utility and the various special funds established by bond covenants. The covenants provide that the revenue of the Utility is to be used first to pay operating and maintenance expenses of the system and second to establish and maintain the special funds. Remaining revenues may then be used for any lawful purpose. The covenants also contain provisions which, among other items, restrict the issuance of additional revenue bonds unless the special funds noted above contain the required amounts and certain financial ratios are met. The Utility is in compliance with all significant financial requirements as of December 31, 2007.

At December 31, 2007, the special funds consisted of the following:

	Cash and Cash Equivalents	Noncurrent Investments	Total
Bond Sinking Fund	\$ 131,125	\$ -	\$ 131,125
Bond Reserve Fund	-	1,584,260	1,584,260
Bond Improvement Fund	-	751,325	751,325
Total Restricted Net Assets	\$ 131,125	\$ 2,335,585	\$ 2,466,710

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 8 – BONDS PAYABLE (Continued)

Monthly deposits into two bond sinking funds are required to establish the amount necessary to pay the next installments of principal and interest on the 2000 and 2004 Electric Revenue Bonds. Bond reserve funds for the 2000 and 2004 Electric Revenue Bonds equaled the required balance at December 31, 2007; therefore monthly deposits into the fund are not currently required. These funds may be used to pay principal and interest payments when insufficient funds are available in the sinking fund.

The bond improvement fund balance at December 31, 2007 equaled the minimum balance required; therefore monthly deposits into the fund are not currently required. These funds are to be used first for principal and interest payments when insufficient funds are available in the sinking and reserve funds and second for extraordinary unbudgeted maintenance expenses or system repairs, renewals and replacements.

Note 9 - RATE MATTERS

Rates of the Utility are established by the Board of Trustees and, as a municipal system, are not subject to the regulation of the Utilities Division of the Department of Commerce of the State of Iowa.

Note 10 - NUMBER OF METER CONNECTIONS

The number of meter connections totaled 5,883 at December 31, 2007.

Note 11 - LEASES

The Utility leases electrical generation capacity of a jet turbine generator, its share of the Neal 4 plant, its share of the Wisdom 2 plant, and its share of the Walter Scott 4 plant under operating leases to other utilities or their associations. The revenues from such leases are classified as leased facilities. The Utility's investment in these facilities is included in capital assets in service and is set forth as follows:

Jet turbine generator	\$ 2,562,957
Neal 4 plant	4,864,807
Wisdom 2 plant	2,314,530
Walter Scott 4 plant	<u>14,221,849</u>
Total	23,964,143
Less accumulated depreciation	<u>6,243,170</u>
Net investment	<u>\$ 17,720,973</u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 11 - LEASES (Continued)

The lease of the Neal 4, Walter Scott 4 and Wisdom 2 plant are long-term commitment based on capacity. The amount is determined by formula based on usage and totaled \$457,906, \$409,349 and \$20,890, respectively, in 2007. The leases of the jet turbine generator are both by non-cancelable lease and a variable lease determined by capacity and totaled \$161,991 in 2007. The following is a schedule of future minimum rentals on non-cancelable operating leases on the jet turbine generator as of December 31, 2007:

2008	65,000
2009	65,000
2010	65,000
2011	65,000
	<hr/>
Total minimum lease payment receivable	<u>\$ 260,000</u>

The Utility leases bandwidth, property, and building space to the Water Utility and Communications Utility. The revenues from such leases are classified as leased facilities and totaled \$432,347 in 2007. The leases are 20-year variable leases based on bandwidth and space utilized. No amount is payable at December 31, 2007.

The Utility leases building space from the Water Utility. The expense from the lease is classified as operating expense. The lease is a monthly lease based on building space utilized and totaled \$8,004 in 2007. No amount is payable at December 31, 2007.

Note 12 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 3.70% through June 30, 2007 and 3.90% presently of their annual salary and the Utility was required to contribute 5.75% through June 30, 2007 and 6.05% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2007, 2006 and 2005 were \$95,983, \$87,914, and \$85,741, respectively, equal to the required contributions for each year.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 12 - RETIREMENT SYSTEM (Continued)

Employees Pension Plan

All full-time employees of the Electric Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Electric Utility's contribution to the 457b Pension Plan for 2007 totaled \$140,609.

Note 13 - RISK MANAGEMENT

The Electric Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limits. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. The Utility, as is typical in the electric power industry, does not insure its transmission lines due to the high cost of such coverage.

Note 14 - RELATED PARTIES

The Electric Utility, Water Utility and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Notes 7 and 11.

Note 15 - COMMITMENTS

During 2005, the Electric Utility provided a letter of support to continue funding Iowa Great Lakes Corridor of Opportunity at a level of \$12,500 per year for four years.

Beginning in 2009, the Electric Utility pledged support to the Iowa Great Lakes Corridor of Opportunity at a level of \$25,000 per year for four years. This commitment is subject to annual review by the Utility Board.

During 2008, the Electric Utility pledged support of cash or in kind for the Streetlights on the Grand Avenue Project from 8th to 18th up to \$625,000.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 15 – COMMITMENTS (Continued)

During 2007, the Electric Utility entered into an agreement to purchase a 1.23% ownership in the generating facilities at Sutherland Generating Station Unit 4. The plant is estimated to be in production in 2013. The commitment of Spencer Municipal Utilities, in order to maintain its percentage of ownership, is expected to approximate \$19,480,000. This commitment is contingent upon the State of Iowa issuing a permit for the plant. This permit is expected to be issued during the summer of 2008. Approximately \$4,782 had been paid or accrued resulting in a future commitment of approximately \$19,475,218. Future payments by the Utility will be required as construction progresses.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2007**

	Budgeted Amounts		Actual	Final to Actual Variance
	Original	Amended		
Receipts:				
Municipal Electric Utility			\$ 15,994,228	
Municipal Water Utility			1,320,616	
Municipal Communications Utility			6,599,428	
Total Receipts	\$ 23,283,750	\$ 29,716,000	23,914,272	\$ 5,801,728
Expenditures:				
Municipal Electric Utility			15,609,082	
Municipal Water Utility			1,790,857	
Municipal Communications Utility			6,158,476	
Total Expenditures	25,284,755	28,744,756	23,558,415	5,186,341
Excess (Deficiency) of Revenues Over Expenditures	(2,001,005)	971,244	355,857	615,387
Other Financing Sources (Uses);				
Transfers In	-	-	-	-
Transfers Out	(2,350,000)	(2,350,000)	-	(2,350,000)
Total Other Financing Sources (Uses)	(2,350,000)	(2,350,000)	-	(2,350,000)
Net Change in Net Assets	(4,351,005)	(1,378,756)	355,857	(1,734,613)
Net Assets at Beginning of Year	28,536,464	28,536,464	23,105,416	5,431,048
Net Assets at End of Year	\$ 24,185,459	\$ 27,157,708	\$ 23,461,273	\$ 3,696,435

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2007**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 15,994,228	\$ (2,670,425)	\$ 13,323,803
Municipal Water Utility	\$ 1,320,616	(36,646)	1,283,970
Municipal Communications Utility	\$ 6,599,428	4,268,716	10,868,144
Total Receipts	<u>23,914,272</u>	<u>1,561,645</u>	<u>25,475,917</u>
Expenditures:			
Municipal Electric Utility	15,609,082	(3,789,793)	11,819,289
Municipal Water Utility	1,790,857	(521,514)	1,269,343
Municipal Communications Utility	6,158,476	(1,110,895)	5,047,581
Total Expenditures	<u>23,558,415</u>	<u>(5,422,202)</u>	<u>18,136,213</u>
Net Change in Net Assets	355,857	6,983,847	7,339,704
Net Assets at Beginning of Year	<u>23,105,416</u>	<u>43,419,545</u>	<u>66,524,961</u>
Net Assets at End of Year	<u>\$ 23,461,273</u>	<u>\$ 50,403,392</u>	<u>\$ 73,864,665</u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2007**

The budgetary comparison is presented as Required Supplementary Information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for each individual utility.

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

Formal and legal budgetary control is based upon nine major classes of disbursements, known as functions, not by fund. These functions are public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, and business type activities. All Utility disbursements are included in business type activities function and are required to be budgeted. During the year, one budget amendment increased budgeted disbursements by \$3,460,001. This budget amendment is reflected in the final budgeted amounts.

THIS PAGE INTENTIONALLY LEFT BLANK

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE
AND INTERNAL CONTROL OVER FINANCIAL REPORTING**

Board of Trustees
Spencer Municipal Utilities – Municipal Electric Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of Municipal Electric Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2007, which collectively comprise Spencer Municipal Utility's financial statements listed in the table of contents, and have issued our report thereon dated April 10, 2008. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Spencer Municipal Utility's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood a misstatement of Spencer Municipal Utility's financial statements that is more than inconsequential will not be prevented or detected by Spencer Municipal Utility's internal control. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings and as item II-A-07 to be significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies that result in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by Spencer Municipal Utility's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiency described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Comments involving statutory and other legal matters about the Spencer Municipal Utility's operations for the year ended December 31, 2007, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of Spencer Municipal Utility. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Spencer Municipal Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Spencer and other parties to whom Spencer Municipal Utilities may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utilities during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 10, 2008

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL ELECTRIC UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2007**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) Significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements, including material weakness.
- (c) The audit did not disclose any noncompliance, which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-07 Financial Reporting – During the audit, we identified material adjustments or adjustments which could result in material amounts of capital assets not initially identified by Spencer Municipal Utility's internal control. These amounts were either not recorded or not properly recorded in Spencer Municipal Utility's financial statements. Adjustments were subsequently made by Spencer Municipal Utility, if applicable, to properly include or reclassify these amounts in the financial statements.

Recommendation – Spencer Municipal Utility should implement procedures to ensure all capital assets are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response – We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL ELECTRIC UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2007**

Part III: Other Findings Related to Required Statutory Reporting

III-A-07 Certified Budget – Disbursements during the year ended December 31, 2007 did not exceed the amounts budgeted in the business type activities function.

III-B-07 Questionable Expenditures – No expenditures were noted which did not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-07 Travel Expenses – No expenditures of the Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-07 Business Transactions – Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Tom Howe, Board Member Part owner of H & N Chevrolet	Maintenance & Repairs	\$ 665
Dave Hultgren, Board Member Owner, Northwest Equipment	Maintenance & Repairs	\$ 399
Rachel, Rebecca and Ryan Florke Children of employee	Cleaning Services	\$ 2,850

In accordance with Chapter 362.5(10) of the Code of Iowa, the transactions with Board Members Howe and Hultgren and for cleaning services do not appear to represent conflicts of interest since total transactions with each were less than \$1,500 during the year.

III-E-07 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-07 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-07 Revenue Bonds – As of December 31, 2007, the Utility had complied with all significant financial requirements related to its Electric Revenue Bonds, Series 2000, and Electric Revenue Bonds, Series 2004.

III-H-07 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

SPENCER MUNICIPAL UTILITIES

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA**

THIS PAGE INTENTIONALLY LEFT BLANK

WILLIAMS & COMPANY P.C.

Certified Public Accountants

Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Water Utility
Spencer, IA 51301

We have audited the accompanying balance sheets of the Municipal Water Utility of the City of Spencer, Iowa (the Utility) as of December 31, 2007 and 2006, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Utility's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Utility as of December 31, 2007 and 2006, and the respective changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 10, 2008 on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis and budgetary comparison information on pages 31 through 33 and 48 through 50 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurements and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 10, 2008

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of management's discussion and analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Water Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the year ended December 31, 2007.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2007 Financial Highlights

The Utility delivered approximately 470,289,000 gallons of water to its retail customers in 2007 compared to approximately 471,755,000 gallons in 2006.

The Utility's net assets increased by \$14,627 to \$7,264,448 as a result of operations for the year ended December 31, 2007.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Balance Sheet

	<u>2007</u>	<u>2006</u>
Current assets	\$2,338,416	\$2,852,802
Capital assets, net of depr.	5,280,711	4,924,548
Noncurrent assets	1,197,949	1,195,189
Deferred costs	<u>11,872</u>	<u>13,096</u>
Total assets	<u>8,828,948</u>	<u>8,985,635</u>
Current liabilities	491,500	597,814
Long-term debt	<u>1,091,000</u>	<u>1,156,000</u>
Total liabilities	<u>1,582,500</u>	<u>1,753,814</u>
Investments in capital assets, net of related debt	4,124,711	3,705,548
Restricted	197,949	195,189
Unrestricted	<u>2,923,788</u>	<u>3,331,084</u>
Total net assets	<u>7,246,448</u>	<u>7,231,821</u>
Total liabilities and net assets	<u>\$8,828,948</u>	<u>\$8,985,635</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Sales of water	\$1,087,145	\$984,667
Other	<u>24,856</u>	<u>33,243</u>
Total operating revenue	<u>1,112,001</u>	<u>1,017,910</u>
System operation & maintenance	743,628	653,296
Depreciation & amortization	302,256	297,662
Customer service & administration	<u>127,978</u>	<u>119,372</u>
Total operating expenses	<u>1,173,862</u>	<u>1,070,330</u>
Operating loss	(61,861)	(52,420)
Interest income	140,981	112,253
Interest expense	(45,198)	(47,591)
Other income (expense)	<u>(19,295)</u>	<u>76,781</u>
Total non-operating revenues	<u>76,488</u>	<u>141,443</u>
Change in net assets	14,627	89,023
Net assets, beginning of year	<u>7,231,821</u>	<u>7,142,798</u>
Net assets, end of year	<u>\$7,246,448</u>	<u>\$7,231,821</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Financial Analysis

The Utility's total assets decreased by approximately \$156,000.

The Utility's gross revenues increased by approximately \$95,000 or 9.24%.

Total operating expenses increased by approximately \$103,500 due to increased expenses related to the water plant operation and maintenance and distribution maintenance.

Total operating loss generated in 2007 was \$61,861 compared to \$52,420 in 2006.

Contributions in Aid of Construction totaled \$6,196 for the year ended December 31, 2007 compared to \$105,614 for the year ended December 31, 2006.

The Utility had a net income of \$14,627 for the year ended December 31, 2007 compared to \$89,024 for the year ended December 31, 2006.

Capital Assets and Debt Administration

Net capital assets increased by approximately \$355,000 due to construction of water mains and purchase of capital assets during the year ended December 31, 2007.

Economic Factors

During the year ended December 31, 2007, the Utility experienced a net income of \$14,627. Because net operating expenses exceeding operating revenue, the Board of Trustees adopted a rate adjustment effective with consumption beginning April 28, 2008. This rate adjustment will increase revenues by approximately \$140,000.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Business Manager, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

THIS PAGE INTENTIONALLY LEFT BLANK

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
BALANCE SHEETS
DECEMBER 31, 2007 AND 2006**

	2007	2006
ASSETS		
Capital Assets:		
Plant in Service	\$ 10,865,765	\$ 10,118,054
Accumulated Depreciation	(5,868,854)	(5,566,598)
Net Plant in Service	4,996,911	4,551,456
Land	258,533	258,533
Construction in Progress	25,267	114,559
Total Capital Assets	5,280,711	4,924,548
Noncurrent Assets:		
Cash and Cash Equivalents		
Restricted	197,949	195,189
Noncurrent Investments		
Board Designated	1,000,000	1,000,000
Total Noncurrent Assets	1,197,949	1,195,189
Current Assets:		
Cash and Cash Equivalents		
Unrestricted	(91,719)	381,282
Board Designated	2,098,106	2,098,106
Accounts Receivable (Net of Allowance for Doubtful		
Accounts of \$10,000 and \$5,000)	215,762	241,894
Unbilled Usage	41,135	37,494
Materials And Supplies Inventory	67,151	87,502
Prepayments and Other	7,981	6,524
Total Current Assets	2,338,416	2,852,802
Deferred Costs:		
Unamortized Bond Issue Costs	11,872	13,096
Total Assets	\$ 8,828,948	\$ 8,985,635

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
BALANCE SHEETS
DECEMBER 31, 2007 AND 2006**

	2007	2006
LIABILITIES AND NET ASSETS		
Bonds Payable:		
Bonds Payable	1,156,000	1,219,000
Less - Current Maturities	(65,000)	(63,000)
Total Bonds Payable	<u>1,091,000</u>	<u>1,156,000</u>
Current Liabilities:		
Accounts Payable	391,457	484,196
Payroll and Sales Tax Payable	8,485	14,315
Accrued Payroll and Compensated Absences	18,998	28,341
Accrued Interest Payable	7,560	7,962
Current Maturities of Long-Term Debt	65,000	63,000
Total Current Liabilities	<u>491,500</u>	<u>597,814</u>
Total Liabilities	<u>1,582,500</u>	<u>1,753,814</u>
Net Assets		
Invested in Capital Assets, Net of Related Debt	4,136,583	3,718,644
Restricted	197,949	195,189
Unrestricted	2,911,916	3,317,988
Total Net Assets	<u>7,246,448</u>	<u>7,231,821</u>
Total Liabilities and Net Assets	<u><u>\$ 8,828,948</u></u>	<u><u>\$ 8,985,635</u></u>

THIS PAGE INTENTIONALLY LEFT BLANK

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	2007	2006
Operating Revenues:		
Residential	\$ 864,836	\$ 782,464
Commercial	222,309	202,203
Rental Income	23,746	32,872
Miscellaneous	1,110	371
Total Operating Revenues	1,112,001	1,017,910
Operating Expenses:		
Treatment	427,851	383,420
Distribution	315,777	269,876
Depreciation and Amortization	302,256	297,662
Customer Operations	56,993	52,175
General and Administrative	70,985	67,197
Total Operating Expenses	1,173,862	1,070,330
Operating Loss	(61,861)	(52,420)
Non-Operating Income (Expense):		
Interest Income on Investments	140,981	112,253
Contributions From Developers	6,196	105,614
Leased Facilities	22,923	9,141
Interest Expense	(45,198)	(47,591)
Bond Amortization Expense	(1,224)	(1,224)
Inventory Sales	1,869	-
Gain on Plant Retirements	-	8,190
Payment in Lieu of Property Taxes	(49,059)	(44,940)
Total Non-Operating Income (Expense)	76,488	141,443
Change in Net Assets	14,627	89,023
Net Assets at Beginning of Year	7,231,821	7,142,798
Net Assets at End of Year	\$ 7,246,448	\$ 7,231,821

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	<u>2007</u>	<u>2006</u>
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 1,154,843	\$ 936,887
Cash Payments to Suppliers for Goods and Services	(894,817)	(757,824)
Cash Payments to Employees for Services	(86,158)	(69,021)
Payments Received From Leasing of Facilities	22,923	9,141
	<hr/>	<hr/>
Net Cash Provided By Operating Activities	196,791	119,183
	<hr/>	<hr/>
Cash Flows From Noncapital Financing Activities:		
Payment in Lieu of Property Taxes	(49,059)	(44,940)
	<hr/>	<hr/>
Net Cash (Used) By Noncapital Financing Activities	(49,059)	(44,940)
	<hr/>	<hr/>
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(652,223)	(509,733)
Cash Received from Sale of Land	-	9,000
Revenue Bond Principal Repayment	(63,000)	(61,000)
Payments Received From Sale of Inventory	1,869	-
Interest Paid	(45,600)	(47,980)
	<hr/>	<hr/>
Net Cash (Used) By Capital and Related Financing Activities	(758,954)	(609,713)
	<hr/>	<hr/>
Cash Flows From Investing Activities:		
Interest Received From Investments	140,981	112,253
	<hr/>	<hr/>
Net Cash Provided By Investing Activities	140,981	112,253
	<hr/>	<hr/>
Net (Decrease) in Cash	(470,241)	(423,217)
	<hr/>	<hr/>
Cash at Beginning of Year	2,674,577	3,097,794
	<hr/>	<hr/>
Cash at End of Year	\$ 2,204,336	\$ 2,674,577
	<hr/>	<hr/>
Reconciliation:		
Cash and Cash Equivalents		
Unrestricted	\$ (91,719)	\$ 381,282
Restricted	197,949	195,189
Board Designated	2,098,106	2,098,106
	<hr/>	<hr/>
	\$ 2,204,336	\$ 2,674,577
	<hr/>	<hr/>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	2007	2006
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating Loss	\$ (61,861)	\$ (52,420)
Adjustments to Reconcile Operating Income to Net Cash Provided By Operating Activities		
Depreciation and Amortization	302,256	297,662
Leased Facilities Income	22,923	9,141
(Increase) Decrease in Operating Assets:		
Accounts Receivable	26,132	(51,825)
Unbilled Usage	(3,641)	(3,483)
Materials and Supplies Inventory	20,351	(25,715)
Prepayments	(1,457)	661
Increase (Decrease) in Operating Liabilities:		
Accounts Payable	(92,739)	(60,121)
Accrued Payroll and Compensated Absences	(9,343)	(1,824)
Accrued Expenses	(5,830)	7,107
Total Adjustments	258,652	171,603
Net Cash Provided By Operating Activities	\$ 196,791	\$ 119,183

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Water Utility of the City of Spencer, Iowa (Water Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Electric Utility and the Municipal Communication Utility of the City of Spencer, Iowa by a five member Board of Trustees.

The Utility follows the accounting practices prescribed through the Federal Energy Regulatory Commission for regulated utilities and proprietary fund accounting for governmental entities under accounting principles generally accepted in the United States of America.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes. An audit of the City of Spencer for the year ended June 30, 2007 has been completed and is filed under separate cover.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new water facilities. In addition, net interest costs on construction debt are capitalized.

Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred.

Depreciation is provided on a straight-line basis. Current depreciation expense is approximately 2.84% of the original cost of depreciable water plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	40 years
Buildings and Equipment	5-20 years
Vehicles	5 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Bond Issue Costs

Unamortized debt issue costs are amortized over the life of the debt on a straight line basis which approximates the effective interest method.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent debt when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The Utility's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

G. Income Taxes

The Water Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of water. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2007, totaled \$41,135.

I. Estimates

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS

The Utility's deposits in bank at December 31, 2007 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

The Utility had investments in Iowa Public Agency Investment Trust which are valued at an amortized cost of \$1,309,858 pursuant to Rule 2a-7 under the Investment Company Act of 1940.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS (Continued)

Interest Rate Risk – The Utility’s investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

Credit Risk – The Utility’s investment in the Iowa Public Agency Investment Trust is unrated.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

Investments are recorded at cost which approximates market. Adjustments are made to cost for any premium or discount, which is amortized over the maturity of the investment. Adjustments are also made to account for the change in accrued interest on respective investments.

Reconciliation of the Utility’s cash and cash equivalents and noncurrent investments is as follows:

	2007	2006
Cash and cash equivalents:		
Board designated	\$ 2,098,106	\$ 2,098,106
Restricted	197,949	195,189
Unrestricted	(91,719)	381,282
Total cash and cash equivalents	<u>2,204,336</u>	<u>2,674,577</u>
Noncurrent investments:		
Board designated	<u>1,000,000</u>	<u>1,000,000</u>
Total noncurrent investments	<u>1,000,000</u>	<u>1,000,000</u>
Total cash and cash equivalents and noncurrent investments	<u>\$ 3,204,336</u>	<u>\$ 3,674,577</u>

Note 3 - BOARD DESIGNATED FUNDS

The Board of trustees of the Utility has designated certain funds to be placed in a contingency reserve account. These funds, which are from unrestricted net assets, are being designated for contingencies such as a natural disaster and cannot be expended without Board approval.

The Board of Trustees of the Utility has designated certain funds to be placed in a replacement and construction reserve account. These funds, which are from unrestricted net assets, are being designated for replacement of property, plant, and equipment and for new construction. These funds cannot be expended without Board approval.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 3 - BOARD DESIGNATED FUNDS (Continued)

Assets of the funds as of December 31, 2007 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Cash and cash equivalents	\$ 469,106	\$ 1,629,000	\$ 2,098,106
Noncurrent investments	-	1,000,000	1,000,000
Total	\$ 469,106	\$ 2,629,000	\$ 3,098,106

Note 4 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2007 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 258,533	\$ -	\$ -	\$ 258,533
Construction in progress	114,559	454,712	(544,004)	25,267
Total capital assets not being depreciated	373,092	454,712	(544,004)	283,800
Capital assets being depreciated:				
Infrastructure	6,187,916	555,047	-	6,742,963
Buildings and equipment	3,779,229	192,664	-	3,971,893
Vehicles	150,909	-	-	150,909
Total capital assets being depreciated	10,118,054	747,711	-	10,865,765
Less accumulated depreciation	5,566,598	302,256	-	5,868,854
Total capital assets being depreciated - net	4,551,456	445,455	-	4,996,912
Capital assets - net	\$ 4,924,548	\$ 900,167	\$ (544,004)	\$ 5,280,711

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 5 - SEWER, STORM WATER, AND SOLID WASTE

The Electric Utility bills and collects sewer, storm water, and solid waste revenues for the City of Spencer. The resulting receivable and corresponding payable are recorded under the Water Utility. The City of Spencer reimburses the Electric Utility for these services.

Note 6 - TRANSFERS IN LIEU OF PROPERTY TAXES

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Currently, transfers approximate 5% of gross sales. Additionally, funds declared to be surplus can be, and have been, transferred to the City.

Note 7 - BONDS PAYABLE

Bonds payable activity for the year ended December 31, 2006 was as follows:

	Beginning			Ending	Amounts
	Balance	Additions	Reductions	Balance	Due Within One Year
Series 2001 revenue bonds	\$1,219,000	\$ -	\$ 63,000	\$1,156,000	\$ 65,000
Total revenue bonds	\$1,219,000	\$ -	\$ 63,000	\$1,156,000	\$ 65,000

The Series 2000 revenue bonds require annual principal payments, due December 1, and semiannual interest payments, due June 1 and December 1. Interest rate throughout the term of the bonds is 3.84%. The bonds are secured by the future net revenues of the Utility. Long-term debt matures and bears interest as follows:

	Series 2000	
	Principal	Interest
2008	\$ 65,000	\$ 44,390
2009	68,000	41,894
2010	70,000	39,283
2011	73,000	36,595
2012	76,000	33,792
2013-2017	426,000	122,880
2018-2021	378,000	35,558
Total	\$ 1,156,000	\$ 354,392

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 7 – BONDS PAYABLE (Continued)

The bond resolutions provide certain covenants relating to the collection, segregation, and distribution of revenues from customers; places certain restrictions on future borrowing and leasing or disposition of assets; and requires that minimum insurance coverage be maintained.

Restricted Funds

Outstanding Water Revenue Bonds are collateralized by the revenue of the Utility and the various special funds established by bond covenants. The covenants provide that the revenue of the Utility is to be used first to pay operating and maintenance expenses of the system and second to establish and maintain the special funds. Remaining revenues may then be used for any lawful purpose. The covenants also contain provisions which, among other items, restrict the issuance of additional revenue bonds unless the special funds noted above contain the required amounts and certain financial ratios are met. The Utility is in compliance with all significant financial requirements as of December 31, 2007.

At December 31, 2007, the special funds consisted of the following:

	<u>Total</u>
Bond Sinking Fund	\$ 82,949
Bond Reserve Fund	<u>115,000</u>
Total	<u>\$ 197,949</u>

Monthly deposits into the bond sinking fund are required to establish the amount necessary to pay the next installments of principal and interest. The bond reserve fund at December 31, 2007 equaled the required balance; therefore monthly deposits into the fund are not currently required. These funds may be used to pay principal and interest payments when insufficient funds are available in the sinking fund.

Note 8 - RATE MATTERS

Rates of the Utility are established by the Board of Trustees and, as a municipal system, are not subject to the regulation of the Utilities Division of the Department of Commerce of the State of Iowa.

Note 9 - NUMBER OF METER CONNECTIONS

The number of meter connections totaled 5,611 at December 31, 2007.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 10 - LEASES

The Utility leases building space to the Electric Utility and Communications Utility. The revenues from such leases are classified as leased facilities. The leases are monthly leases based on building space utilized and totaled \$10,803 in 2007. No amount is receivable at December 31, 2007.

The Utility lease bandwidth and building space from the Electric and Communications Utilities. The expense from such leases is classified as operating expense. The lease is a 20-year variable lease based on bandwidth and space utilized and totaled \$23,035 in 2007. No amount is payable at December 31, 2007.

Note 11 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing, multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan member and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 3.70% through June 30, 2007 and 3.90% presently of their annual salary and the Utility was required to contribute 5.75% through June 30, 2007 and 6.05% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2007, 2006 and 2005 were \$11,545, \$15,922 and \$14,133, respectively, equal to the required contributions for each year.

EMPLOYEES PENSION PLAN

All full-time employees of the Water Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Water Utility's contribution to the Money Accumulation Pension Plan for 2007 totaled \$14,722.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 12 - RISK MANAGEMENT

The Water Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 13 - RELATED PARTIES

The Electric Utility, Water Utility, and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Note 10.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
SCHEDULE OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCE, BUDGET AND ACTUAL, ALL
GOVERNMENTAL FUNDS AND PROPRIETARY FUND - CASH BASIS
FOR YEAR ENDED DECEMBER 31, 2007**

	Budgeted Amounts		Actual	Final to Actual Variance
	Original	Amended		
Receipts:				
Municipal Electric Utility			\$ 15,994,228	
Municipal Water Utility			1,320,616	
Municipal Communications Utility			6,599,428	
Total Receipts	\$ 23,283,750	\$ 29,716,000	23,914,272	\$ 5,801,728
Expenditures:				
Municipal Electric Utility			15,609,082	
Municipal Water Utility			1,790,857	
Municipal Communications Utility			6,158,476	
Total Expenditures	25,284,755	28,744,756	23,558,415	5,186,341
Excess (Deficiency) of Revenues Over Expenditures	(2,001,005)	971,244	355,857	615,387
Other Financing Sources (Uses);				
Transfers In	-	-	-	-
Transfers Out	(2,350,000)	(2,350,000)	-	(2,350,000)
Total Other Financing Sources (Uses)	(2,350,000)	(2,350,000)	-	(2,350,000)
Net Change in Net Assets	(4,351,005)	(1,378,756)	355,857	(1,734,613)
Net Assets at Beginning of Year	28,536,464	28,536,464	23,105,416	5,431,048
Net Assets at End of Year	\$ 24,185,459	\$ 27,157,708	\$ 23,461,273	\$ 3,696,435

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2007**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 15,994,228	\$ (2,670,425)	\$ 13,323,803
Municipal Water Utility	\$ 1,320,616	(36,646)	1,283,970
Municipal Communications Utility	\$ 6,599,428	4,268,716	10,868,144
Total Receipts	<u>23,914,272</u>	<u>1,561,645</u>	<u>25,475,917</u>
Expenditures:			
Municipal Electric Utility	15,609,082	(3,789,793)	11,819,289
Municipal Water Utility	1,790,857	(521,514)	1,269,343
Municipal Communications Utility	6,158,476	(1,110,895)	5,047,581
Total Expenditures	<u>23,558,415</u>	<u>(5,422,202)</u>	<u>18,136,213</u>
 Net Change in Net Assets	 355,857	 6,983,847	 7,339,704
Net Assets at Beginning of Year	<u>23,105,416</u>	<u>43,419,545</u>	<u>66,524,961</u>
Net Assets at End of Year	<u>\$ 23,461,273</u>	<u>\$ 50,403,392</u>	<u>\$ 73,864,665</u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2007**

The budgetary comparison is presented as Required Supplementary Information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for each individual utility.

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

Formal and legal budgetary control is based upon nine major classes of disbursements, known as functions, not by fund. These functions are public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects and business type activities function and are required to be budgeted. During the year, one budget amendment increased budgeted disbursements by \$3,460,001. This budget amendment is reflected in the final budgeted amounts.

THIS PAGE INTENTIONALLY LEFT BLANK



Certified Public Accountants

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND INTERNAL CONTROL OVER FINANCIAL REPORTING

Board of Trustees
Spencer Municipal Utilities – Municipal Water Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of Municipal Water Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2007, which collectively comprise Spencer Municipal Utility's financial statements listed in the table of contents, and have issued our report thereon dated April 10, 2008. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Spencer Municipal Utility's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood a misstatement of Spencer Municipal Utility's financial statements that is more than inconsequential will not be prevented or detected by Spencer Municipal Utility's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies that result in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by Spencer Municipal Utility's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Comments involving statutory and other legal matters about the Spencer Municipal Utility's operations for the year ended December 31, 2007, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of Spencer Municipal Utility. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Spencer Municipal Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Spencer and other parties to whom Spencer Municipal Utilities may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utilities during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 10, 2008

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL WATER UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2007**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) The audit did not disclose any significant deficiencies in internal control over financial reporting, including material weaknesses to the financial statements.
- (c) The audit did not disclose any noncompliance, which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCIES:

No matters were reported.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL WATER UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2007**

Part III: Other Findings Related to Required Statutory Reporting

III-A-07 Certified Budget -- Disbursements during the year ended December 31, 2007 did not exceed the amounts budgeted in the business type activities function.

III-B-07 Questionable Expenditures -- We noted no expenditures that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-07 Travel Expenses -- No expenditures of Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-07 Business Transactions -- Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Dave Hultgren, Board Member		
Owner, Northwest Equipment	Maintenance & Repairs	\$ 36

In accordance with Chapter 362.5(10) of the Code of Iowa, the transactions with the Board Member do not appear to represent conflicts of interest since total transactions with each were less than \$1,500 during the year.

III-E-07 Bond Coverage -- Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-07 Board Minutes -- No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-07 Revenue Bonds -- As of December 31, 2007, the Utility is in compliance with all significant financial requirements related to its Water Revenue Bond, Series 2000.

III-H-07 Deposits and Investments -- No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA

THIS PAGE INTENTIONALLY LEFT BLANK

INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Communications Utility
Spencer, IA 51301

We have audited the accompanying balance sheets of the Municipal Communications Utility of the City of Spencer, Iowa (the Utility) as of December 31, 2007 and 2006, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Utility's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Utility as of December 31, 2007 and 2006, and the respective changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 10, 2008 on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis and budgetary comparison information on pages 56 through 58 and 70 through 72 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurements and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 10, 2008

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of management's discussion and analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Communications Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the year ended December 31, 2007.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2007 Financial Highlights

Total assets increased by approximately \$1,258,000 which was attributable to an increase in the cash balance, and increase in receivable balances, an investment in Clay County Communications, LLC, a 28E entity, and an increase in unbilled revenues.

Total net assets increased by \$3,855,560, the result of the utility operations.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Balance Sheet

	<u>2007</u>	<u>2006</u>
Current assets	\$6,680,418	\$5,832,195
Capital assets, net of depreciation	5,570,548	5,205,667
Noncurrent assets	<u>720,752</u>	<u>675,199</u>
Total assets	<u>12,971,718</u>	<u>11,713,061</u>
Current liabilities	717,590	768,493
Long-term debt	<u>3,000,000</u>	<u>5,546,000</u>
Total liabilities	<u>3,717,590</u>	<u>6,314,493</u>
Investments in capital assets, net of related debt	2,590,933	(315,152)
Unrestricted	<u>6,663,195</u>	<u>5,713,720</u>
Total net assets	<u>9,254,128</u>	<u>5,398,568</u>
Total liabilities and net assets	<u>\$12,971,718</u>	<u>\$11,713,061</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Cable television revenue	\$1,076,380	\$1,005,714
Telephone revenue	6,450,718	6,076,880
Data revenue	984,012	815,050
Miscellaneous revenue	<u>5,482</u>	<u>7,535</u>
Total operating revenue	<u>8,516,592</u>	<u>7,905,179</u>
System operation & maintenance	2,905,951	2,828,004
Depreciation & amortization	851,444	949,893
Customer service & administration	<u>880,265</u>	<u>696,057</u>
Total operating expenses	<u>4,637,660</u>	<u>4,473,954</u>
Operating income (loss)	3,878,932	3,431,225
Interest income	198,954	142,996
Interest expense	(206,294)	(277,665)
Other income (expense)	<u>(16,032)</u>	<u>278,120</u>
Total non-operating revenues	<u>(23,372)</u>	<u>143,451</u>
Change in net assets	3,855,560	3,574,676
Net assets, beginning of year	<u>5,398,568</u>	<u>1,823,892</u>
Net assets, end of year	<u>\$9,254,128</u>	<u>\$5,398,568</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Financial Analysis

The Utility's total assets increased by approximately \$1,258,000.

The Utility's gross revenues increased by approximately \$611,000 or 7.73%.

Total operating expenses increased by approximately \$164,000 because of increased expenses for cable programming, telephone long distance and an increase in the number of subscribers. Depreciation and amortization expense decreased by approximately \$98,000.

Total operating income generated in 2007 was approximately \$3,878,932 compared to approximately \$3,431,225 in 2006.

The Utility had a net income of \$3,855,560 for the year ended December 31, 2007 compared to \$3,574,676 for the year ended December 31, 2006.

Capital Assets and Debt Administration

Net capital assets increased by approximately \$360,000 due to capital assets purchases for the year ended December 31, 2007.

Economic Factors

The Utility continues to see positive growth in subscriber base and also net income. The Utility will be faced with increased costs of operating due to cable programming contracts.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Business Manager, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

THIS PAGE INTENTIONALLY LEFT BLANK

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
BALANCE SHEETS
DECEMBER 31, 2007 AND 2006**

	2007	2006
ASSETS		
Current Assets:		
Cash and Cash Equivalents	\$ 4,192,154	\$ 3,751,202
Consumer Deposits	42,203	33,229
Accounts Receivable (Net of Allowance for Doubtful Accounts of \$50,000 and \$30,000)	682,186	1,003,334
Unbilled Usage	1,672,103	883,060
Materials And Supplies Inventory	37,997	39,831
Prepayments and Other	53,775	121,539
Total Current Assets	6,680,418	5,832,195
Capital Assets:		
Land	10,342	10,342
Property and Equipment	10,394,919	9,280,160
Accumulated Depreciation	(4,834,713)	(4,084,835)
Total Capital Assets	5,570,548	5,205,667
Deferred Costs:		
Unamortized FAS 51 Costs	20,385	25,181
Noncurrent Assets:		
Long-term Receivables	700,367	650,018
Total Assets	12,971,718	11,713,061
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts Payable	587,192	661,984
Payroll and Sales Tax Payable	23,671	21,768
Accrued Payroll and Compensated Absences	64,524	51,512
Consumer Deposits	42,203	33,229
Total Current Liabilities	717,590	768,493
Notes Payable		
Note Payable	3,000,000	5,546,000
Total Liabilities	3,717,590	6,314,493
Net Assets		
Invested in Capital Assets, Net of Related Debt	2,590,933	(315,152)
Unrestricted	6,663,195	5,713,720
Total Net Assets	9,254,128	5,398,568
Total Liabilities and Net Assets	\$ 12,971,718	\$ 11,713,061

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	2007	2006
Operating Revenues:		
Cable System Revenue	\$ 1,076,380	\$ 1,005,714
Telephone System Revenue	6,450,718	6,076,880
Data Services Revenue	984,012	815,050
Miscellaneous Income	5,482	7,535
Total Operating Revenues	8,516,592	7,905,179
Operating Expenses:		
Plant Specific and Programming	2,905,951	2,828,004
Depreciation and Amortization	851,444	949,893
Customer Services and Marketing	460,124	360,926
General and Administrative	420,141	335,131
Total Operating Expenses	4,637,660	4,473,954
Operating Income	3,878,932	3,431,225
Non-Operating Income (Expense):		
Leased Facilities	165,150	150,475
Net Income from Joint Ventures	22,445	200,118
Economic Development Payment	(20,625)	(20,000)
Interest Income	198,954	142,996
Interest Expense	(206,294)	(277,665)
Loss on Plant Retirements	(1,160)	(11,723)
Payment in Lieu of Property Taxes	(181,842)	(40,750)
Total Non-Operating Income (Expense)	(23,372)	143,451
Changes in Net Assets	3,855,560	3,574,676
Net Assets at Beginning of Year	5,398,568	1,823,892
Net Assets at End of Year	\$ 9,254,128	\$ 5,398,568

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

	<u>2007</u>	<u>2006</u>
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 6,212,879	\$ 7,280,681
Cash Payments to Suppliers for Goods and Services	(1,520,060)	(3,090,498)
Cash Payments to Employees for Services	(418,238)	(335,484)
Payments Received From Leasing of Facilities	187,595	350,593
	<hr/>	<hr/>
Net Cash Provided By Operating Activities	4,462,176	4,205,292
	<hr/>	<hr/>
Cash Flows From Noncapital Financing Activities:		
Contributions Paid for Economic Development	(20,625)	(20,000)
Payment in Lieu of Property Taxes	(181,842)	(40,750)
	<hr/>	<hr/>
Net Cash (Used) By Noncapital Financing Activities	(202,467)	(60,750)
	<hr/>	<hr/>
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(1,215,068)	(535,449)
Proceeds from Sale of Capital Assets	-	1,557
Repayment of Long-term Debt	(2,546,000)	(1,000,000)
	<hr/>	<hr/>
Interest Paid	(206,294)	(277,664)
	<hr/>	<hr/>
Net Cash (Used) By Capital and Related Financing Activities	(3,967,362)	(1,811,556)
	<hr/>	<hr/>
Cash Flows From Investing Activities:		
Other Investments	(50,349)	(472,290)
Interest Received From Investments	198,954	142,996
	<hr/>	<hr/>
Net Cash Provided (Used) By Investing Activities	148,605	(329,294)
	<hr/>	<hr/>
Net Increase in Cash	440,952	2,003,692
	<hr/>	<hr/>
Cash at Beginning of Year	3,751,202	1,747,510
	<hr/>	<hr/>
Cash at End of Year	<u>\$ 4,192,154</u>	<u>\$ 3,751,202</u>

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

**Reconciliation of Operating Income to Net
Cash Provided by Operating Activities**

Operating Income	\$ 3,878,932	\$ 3,431,225
Adjustments to Reconcile Operating Income to Net Cash Provided By Operating Activities		
Depreciation and Amortization	851,444	949,893
Leased Facilities Income	187,595	350,593
(Increase) Decrease in Operating Assets:		
Consumer Deposits	(8,974)	805
Accounts Receivable	323,518	(8,298)
Unbilled Usage	(789,043)	(617,005)
Materials and Supplies Inventory	1,843	5,783
Prepayments	67,764	(30,144)
Increase (Decrease) in Operating Liabilities:		
Accounts Payable	(74,792)	115,916
Accrued Payroll and Compensated Absences	1,903	(353)
Consumer Deposits	13,012	(805)
Accrued Expenses	8,974	7,682
Total Adjustments	<u>583,244</u>	<u>774,067</u>
Net Cash Provided By Operating Activities	<u><u>\$ 4,462,176</u></u>	<u><u>\$ 4,205,292</u></u>

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Communications Utility of the City of Spencer, Iowa (Communications Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Electric Utility and the Municipal Water Utility of the City of Spencer, Iowa, by a five member Board of Trustees. The Utility was formed to engage in the development and operation of a broadband communications system and the marketing of related services such as cable television, telephone, high-speed data communications and other communication products. The Utility's rates are set by its governing board.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes. An audit of the City of Spencer for the year ended June 30, 2007 has been completed and is filed under separate cover.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new communications facilities. In addition, net interest costs on construction debt are capitalized. Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred. Depreciation is calculated on the straight-line basis. Current depreciation expense is approximately 10.15% of the original cost of depreciable communication plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	10-15 years
Buildings and improvements	20 years
Equipment	5-7 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowed based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Deferred Costs

Cable television system costs allocated during construction of the system are being amortized using the straight-line method over the expected life of the cable television plant.

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent debt when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Utility's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

G. Income Taxes

The Communications Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of communications services. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2007, totaled \$1,672,103.

I. Estimates

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Note 2 - CASH AND CASH EQUIVALENTS

The Utility's deposits in banks at December 31, 2007 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies, and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

Interest Rate Risk – The Utility's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 3 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2007 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 10,342	\$ -	\$ -	\$ 10,342
Total capital assets not being depreciated	10,342	-	-	10,342
Capital assets being depreciated:				
Infrastructure	8,267,669	610,519	(66,437)	8,811,751
Buildings and improvements	194,045	503,287	-	697,332
Equipment	818,446	101,263	(33,873)	885,836
Total capital assets being depreciated	9,280,160	1,215,069	(100,310)	10,394,919
Less accumulated depreciation	4,084,835	846,648	(96,770)	4,834,713
Total capital assets being depreciated - net	5,195,325	368,421	(3,540)	5,560,206
Capital assets - net	\$ 5,205,667	\$ 368,421	\$ (3,540)	\$ 5,570,548

Note 4 - TRANSFERS IN LIEU OF PROPERTY TAX

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Funds totaling \$181,842 were transferred to the City during 2007.

Note 5 - LONG-TERM RECEIVABLES

During December 2003, the Utility entered into an agreement with Northern Iowa Communications Partners, LLC (NICP), an Iowa limited liability company, pursuant to the provisions of Chapter 28E of the Code of Iowa. Under this agreement, the Utility, along with other members of NICP, agrees to pay for the use of a shared switch for routing certain telecommunications traffic at rates adopted by NICP. The Utility will share in profits generated or shortfalls incurred through the 28E agreement due to the method used to determine an annual usage fee paid by NICP to the Utility. An NICP member will be responsible for maintaining the financial records related to the 28E agreement. The amount earned but not received by the Utility of \$235,067 is recorded as a receivable.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 5 - LONG-TERM RECEIVABLES (Continued)

During May 2006, the Utility entered into an agreement with Evertek, Inc., an Iowa Corporation, to create Clay County Communications, LLC as a separate legal entity. Clay County Communications shall function as if it were a limited liability company organized under Iowa Code Chapter 490A. The purpose of this agreement and Clay County Communications is to provide wired and/or wireless communications services in Clay County, Iowa. The Utility and Evertek, Inc. each initially contributed \$400,000. During 2007 the Utility and Evertek, Inc. each made an additional contribution \$150,000. The Utility accounts for the joint venture on the equity method, and has recorded the balance of \$465,300 as a receivable.

Note 6 - NOTE PAYABLE

Note payable activity for the year ended December 31, 2007 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Note Payable - Municipal Electric Utility	\$ 5,546,000	\$ -	\$ 2,546,000	\$ 3,000,000	\$ -

The Board of Trustees of the Municipal Electric Utility adopted a resolution on June 14, 1999, pursuant to Section 384.89 City Code of Iowa and Rule 2.5(5) of the rules promulgated by the City Finance Committee, allowing for the advance of funds not to exceed \$8,000,000 to the Municipal Communications Utility to be utilized for the construction and development of the communication system. These funds are to be repaid upon demand and bear a 4.5% per annum interest rate.

Note 7 - LEASES

The Utility leases building space from the Water Utility. The expense from the lease is classified as operating expense. The lease is a monthly lease based on building space utilized and totaled \$1,968 in 2007. No amount is payable at December 31, 2007.

The Utility leases bandwidth, property, and building space from the Electric Utility. The expense from the lease is classified as operating expense. The lease is a 20-year variable lease based on bandwidth and space utilized and totaled \$406,262 in 2007. No amount is payable at December 31, 2007.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 8 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing, multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 3.70% through June 30, 2007 and 3.90% presently of their annual salary and the Utility was required to contribute 5.75% through June 30, 2007 and 6.05% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2007, 2006 and 2005 were \$37126, \$30,094 and \$27,831, respectively, equal to the required contributions for each year.

Employees Pension Plan

All full-time employees of the Communications Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Communications Utility's contribution to the Money Accumulation Pension Plan for 2007 totaled \$54,229.

Note 9 - RISK MANAGEMENT

The Communications Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 10 - RELATED PARTIES

The Electric Utility, Water Utility, and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Notes 5, 6, and 7.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

Note 10 - CONTINGENCIES

In the last two years, the Utility has provided Iowa based telephone numbers to callers who are then connected to a conference call. The Utility maintains these are terminated in Iowa and charges long-distance carriers a fee for terminating access services. The Utility then pays a portion of the revenue to other communication providers who supply a portion of the services. Until 2007 the long-distance carriers have paid these charges to the Utility and the Utility has paid the other communication providers. In 2007, Sprint, has filed a lawsuit alleging that the calls are not terminated in Iowa, and that the Utility is not entitled to the terminating access charges that are billed to them. Sprint and other major long-distance carriers at various times in 2007 have discontinued paying the charges billed. The Utility has also suspended its payments to the other providers pending the outcome of the litigation. The Utility has chosen to reduce account receivables by \$3,794,217 that have not been paid by the major carriers and to reduce accounts payable to the other communication providers by \$1,829,214 for amounts not paid to them. The effect of this is to reduce operating revenue by \$1,965,003.

Note 11 - COMMITMENTS

The Utility has committed to provide annual support of \$21,000 to the Clay Regional Events center during 2008 and 2009. The support is contingent on the Events Center receiving additional support from other area sources and is subject to annual review by the Utility Board.

During 2005, the Communications Utility provided a letter of support to continue funding Iowa Great Lakes Corridor of Opportunity at a level of \$12,500 per year for four years.

Beginning in 2009, the Communications Utility pledged support to the Iowa Great Lakes Corridor of Opportunity at a level of \$25,000 per year for four years. This commitment is subject to annual review by the Utility Board.

During 2007, the Communications Utility entered in a construction contract totaling approximately \$164,183. This project will bury and use fiber optic cable and is scheduled to be completed in 2008. \$122,447 was paid as of December 31, 2007.

During 2007, the Communication Utility entered in a construction contract totaling \$243,130 for construction of HVAC to be completed in 2008. \$128,241 was paid as of December 31, 2007.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2007**

	Budgeted Amounts		Actual	Final to
	Original	Amended		Actual Variance
Receipts:				
Municipal Electric Utility			\$ 15,994,228	
Municipal Water Utility			1,320,616	
Municipal Communications Utility			6,599,428	
Total Receipts	\$ 23,283,750	\$ 29,716,000	23,914,272	\$ 5,801,728
Expenditures:				
Municipal Electric Utility			15,609,082	
Municipal Water Utility			1,790,857	
Municipal Communications Utility			6,158,476	
Total Expenditures	25,284,755	28,744,756	23,558,415	5,186,341
Excess (Deficiency) of Revenues Over Expenditures	(2,001,005)	971,244	355,857	615,387
Other Financing Sources (Uses);				
Transfers In	-	-	-	-
Transfers Out	(2,350,000)	(2,350,000)	-	(2,350,000)
Total Other Financing Sources (Uses)	(2,350,000)	(2,350,000)	-	(2,350,000)
Net Change in Net Assets	(4,351,005)	(1,378,756)	355,857	(1,734,613)
Net Assets at Beginning of Year	28,536,464	28,536,464	23,105,416	5,431,048
Net Assets at End of Year	\$ 24,185,459	\$ 27,157,708	\$ 23,461,273	\$ 3,696,435

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2007**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 15,994,228	\$ (2,670,425)	\$ 13,323,803
Municipal Water Utility	\$ 1,320,616	(36,646)	1,283,970
Municipal Communications Utility	\$ 6,599,428	4,268,716	10,868,144
Total Receipts	<u>23,914,272</u>	<u>1,561,645</u>	<u>25,475,917</u>
Expenditures:			
Municipal Electric Utility	15,609,082	(3,789,793)	11,819,289
Municipal Water Utility	1,790,857	(521,514)	1,269,343
Municipal Communications Utility	6,158,476	(1,110,895)	5,047,581
Total Expenditures	<u>23,558,415</u>	<u>(5,422,202)</u>	<u>18,136,213</u>
Net Change in Net Assets	355,857	6,983,847	7,339,704
Net Assets at Beginning of Year	<u>23,105,416</u>	<u>43,419,545</u>	<u>66,524,961</u>
Net Assets at End of Year	<u>\$ 23,461,273</u>	<u>\$ 50,403,392</u>	<u>\$ 73,864,665</u>

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2007**

The budgetary comparison is presented as Required Supplementary Information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for each individual utility.

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

Formal and legal budgetary control is based upon nine major classes of disbursements, known as functions, not by fund. These functions are public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects and business type activities function and are required to be budgeted. During the year, one budget amendment increased budgeted disbursements by \$3,460,001. This budget amendment is reflected in the final budgeted amounts.

THIS PAGE INTENTIONALLY LEFT BLANK

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE
AND INTERNAL CONTROL OVER FINANCIAL REPORTING**

Board of Trustees
Spencer Municipal Utilities – Municipal Communications Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of Municipal Communications Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2007, which collectively comprise Spencer Municipal Utility's financial statements listed in the table of contents, and have issued our report thereon dated April 10, 2008. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Spencer Municipal Utility's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood a misstatement of Spencer Municipal Utility's financial statements that is more than inconsequential will not be prevented or detected by Spencer Municipal Utility's internal control. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings as item II-A-07 to be significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies that result in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by Spencer Municipal Utility's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiency described above is material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Comments involving statutory and other legal matters about the Spencer Municipal Utility's operations for the year ended December 31, 2007, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of Spencer Municipal Utility. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Spencer Municipal Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Spencer and other parties to whom Spencer Municipal Utilities may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utilities during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.


Certified Public Accountants

Spencer, Iowa
April 10, 2008

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2007**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) Significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements, including material weakness.
- (c) The audit did not disclose any noncompliance, which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-07 Financial Reporting -- During the audit, we identified material adjustments or adjustments which could result in material amounts of a revenue reserve not initially identified by Spencer Municipal Utility's internal control. These amounts were either not recorded or not properly recorded in Spencer Municipal Utility's financial statements. Adjustments were subsequently made by Spencer Municipal Utility, if applicable, to properly include or reclassify these amounts in the financial statements.

Recommendation -- Spencer Municipal Utility should implement procedures to ensure all revenue adjustments are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response -- We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2007**

Part III: Other Findings Related to Required Statutory Reporting

III-A-07 Certified Budget – Disbursements during the year ended December 31, 2007 did not exceed the amounts budgeted in the business type activities function.

III-B-07 Questionable Expenditures – We noted no expenditures that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-07 Travel Expenses – No expenditures of Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-07 Business Transactions – Business transactions between the Utility and Utility officials or employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
--	--------------------------------	---------------

Tom Howe, Board Member Part owner of H & N Chevrolet	Maintenance & Repairs	\$ 287
---	-----------------------	--------

In accordance with Chapter 362 5(10) of the Code of Iowa, the transactions with the Board Member do not appear to represent a conflict of interest since the transactions were less than \$1,500 during the year.

III-E-07 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-07 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-07 Revenue Bonds – No revenue bonds/notes were issued to the Utility.

III-H-07 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

III-I-07 Telecommunication Services – No instances of noncompliance with Chapter 388.10 of the Code of Iowa were noted.